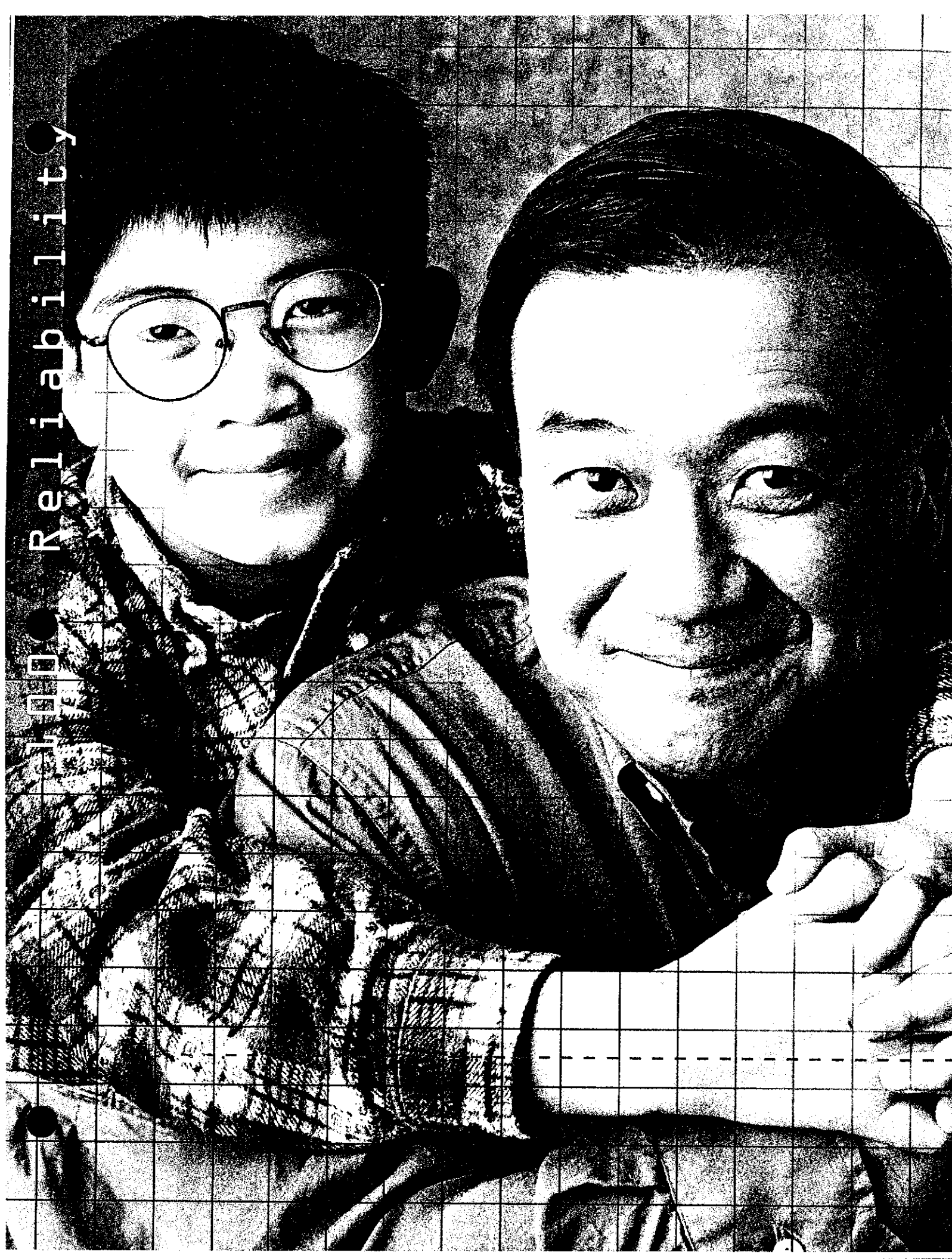


1000 Reliability



## Wireless

Just as the traditional dial tone providers, emergency services suppliers, and their vendors had enhanced 9-1-1 down to a fine science, along comes wireless. Not far behind was the Federal Communications Commission (FCC) mandate requiring the wireless industry to support enhanced 9-1-1 and provide location information to calltakers.

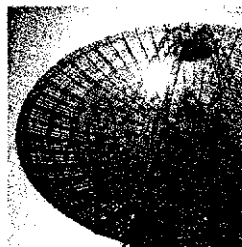
The mandates issued by the FCC in 1996 are referred to as Phase I and Phase II. Phase I location data was to be available as of April 1998 and was to identify the cell sector and callback number of the 9-1-1 caller to the calltaker. Funding for the PSAPs and liability issues for the wireless carriers have significantly slowed Phase I implementation. However, passage of the Wireless Communications and Public Safety Act of 1999 has re-energized deployment efforts, which we hope will bring direct and positive results for our wireless business unit.

The FCC's Phase II implementation schedule has been set for October 1, 2001 and requires wireless carriers to provide more precise caller location information. Through strategic alliances, SCC is well positioned as a leading provider of Phase I and Phase II service to wireless carriers with its 9-1-1Connect<sup>SM</sup> service offerings.

Despite delays and roadblocks experienced in rolling out Phase I, the Wireless business unit accounted for 5% of SCC's total revenue for 1999. The Wireless group announced an increase of 100% in its subscriber base for Phase I services during 1999, bringing total live subscribers to 726,000. The group has carriers representing 27.1 million subscribers under contract.

Continued rollout of Phase I is a priority for SCC's Wireless business unit in 2000, and our strategy for the deployment of our Phase II solution is aggressive. The result is an innovative solution for Phase I and Phase II wireless services, as well as the positioning of SCC as a leading provider of wireless services.

Approximately 98,000  
9-1-1 wireless calls  
are made daily<sup>4</sup>



## The SCC Contribution

You're fly fishing in the streams of the Colorado River, and nothing could be better. You glance over at your friend a few yards behind you and notice that he has collapsed. As you approach, you realize that he is having a heart attack. You grab your wireless phone and dial 9-1-1. You almost establish your location with the calltaker when the call drops, and your connection is lost. With SCC's 911Connect service, the 9-1-1 calltaker has your cell phone number and is able to call you back. Emergency assistance is on the way.

Surveys show 64% of people who buy wireless phones rank safety as their number one priority.<sup>5</sup> SCC understands this importance and is here to provide Phase I and Phase II service to wireless carriers nationwide.

# Emergency roadside assistance services are expected to generate nearly 2.9 billion in annual service revenue <sup>b</sup>

## Building the Future

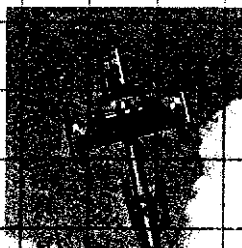
9-1-1 systems were originally designed in the 1970s to support telephones from a fixed location. Calls were delivered and information provided based on a regional or local 9-1-1 system of mapping and call routing. Today, new technologies are introduced that allow mobility; phones are no longer fixed. These technologies include wireless phones, telematics devices in automobiles, and IP telephony. Many provide public safety capability but require a nationwide 9-1-1 system. Routing calls from such devices to the answering point responsible for handling the emergency and delivering the call through the 9-1-1 network present significant challenges that had not been addressed from a national perspective.



SCC recently announced the launch of a revolutionary technology solution for wireless carriers and other non-traditional telecommunications service providers. This new service initiative is the first step toward addressing the challenges and limitations of the nation's aging 9-1-1 system. This offering will provide the ability to properly route and deliver 9-1-1 calls and data throughout the United States. The existing 9-1-1 system that was deployed in local and regional segments is a configuration that seriously limits the ability to efficiently transfer calls outside those boundaries. With the increasing mobility of 9-1-1 callers, this capability is essential on a national scale.



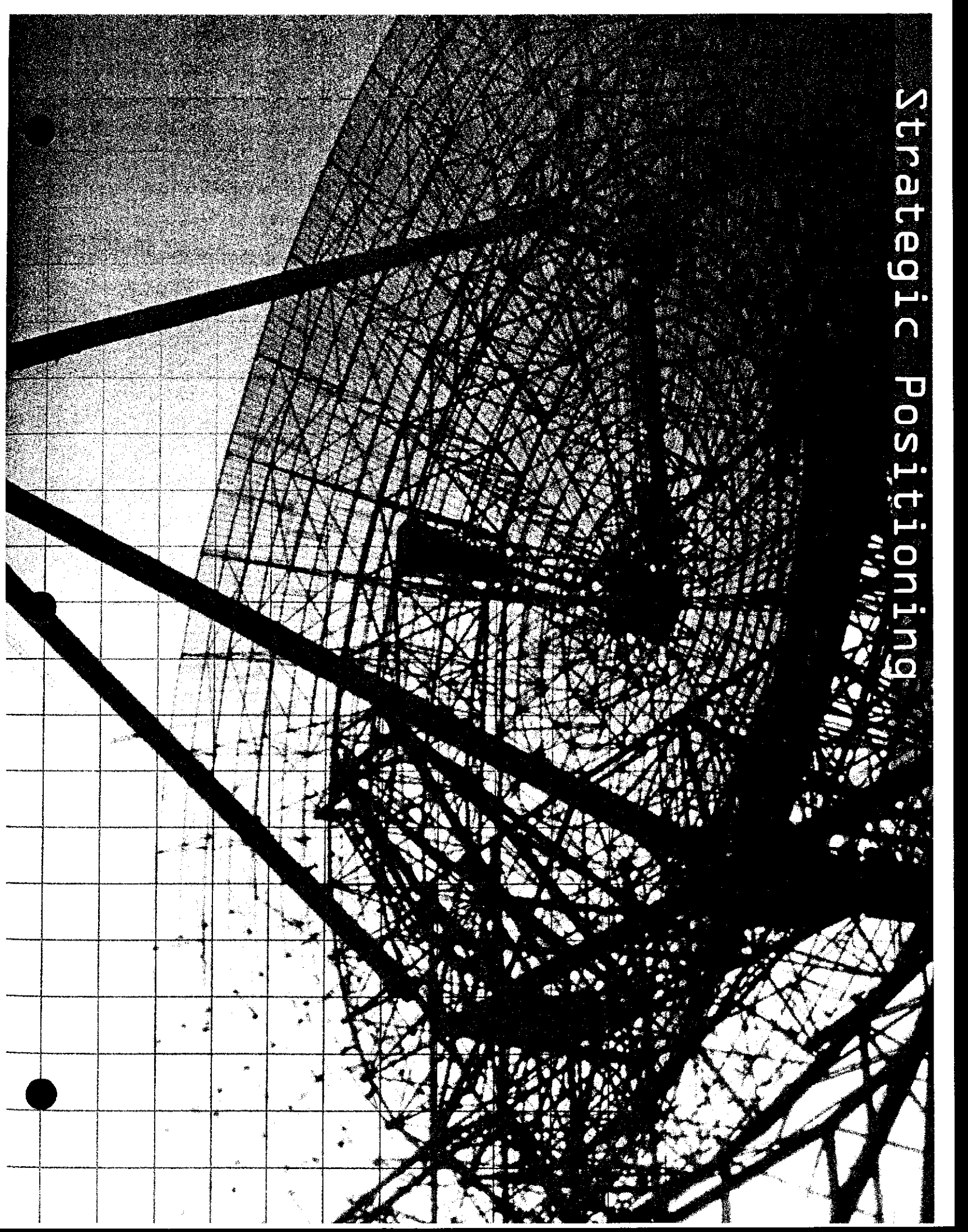
This initiative, 9-1-1 SafetyNet<sup>SM</sup>, will process thousands of boundary updates and new addresses daily. It is designed to easily integrate with the existing 9-1-1 systems and is capable of providing high-speed delivery of voice and data together with automatic call routing information without human intervention. 9-1-1 SafetyNet<sup>SM</sup> was created to meet today's call volumes and network complexities.



9-1-1 SafetyNet will provide a method for a telematics provider to accurately and automatically determine the correct source for emergency services for a stranded motorist, whether the motorist is in Albuquerque or Orlando. Many technologies exist that can determine the exact location of a 9-1-1 caller, but they all need services like SCC's 9-1-1 SafetyNet to determine the proper routing of the call and to deliver the call and data through the 9-1-1 network in seconds, not minutes. 9-1-1 SafetyNet sorts out the confusion of overlapping and multi-jurisdictional locations.

As our society becomes more mobile and the volume of non-traditional subscribers increases, the need for a reliable, state-of-the-art method for providing emergency services will become more critical. SCC's 9-1-1 SafetyNet is a service designed to meet this need for the next generation in service.

# Strategic Positioning



## Selected Financial Data

The following selected financial data are qualified by reference to and should be read in conjunction with our financial statements and notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included herein. The statement of operations data for the years ended December 31, 1999, 1998 and 1997 and the balance sheet data at December 31, 1999 and 1998 are derived from, and are qualified by reference to, the audited financial statements and notes included herein. The statement of operations data for the years ended December 31, 1996 and 1995 and the balance sheet data at December 31, 1997, 1996 and 1995 are derived from audited financial statements not included in this Annual Report.

	D e c e m b e r 3 1 ,				
(dollars in thousands, except per share data)	1999	1998	1997	1996	1995
<b>Revenue:</b>					
Data management services	\$ 32,096	\$ 30,610	\$ 24,005	\$ 13,165	\$ 3,531
Licenses and implementation services	488	3,839	3,067	1,637	3,882
Total revenue	32,584	34,449	27,072	14,802	7,413
<b>Costs and expenses:</b>					
Cost of data management services	24,338	20,740	15,378	7,996	2,840
Cost of licenses and implementation services	138	836	1,283	596	1,041
Sales and marketing	5,314	4,119	3,850	3,204	2,016
General and administrative	4,931	4,959	3,227	1,533	830
Total costs and expenses	34,721	30,654	23,738	13,329	6,727
Income (loss) from operations	(2,137)	3,795	3,334	1,473	686
Other income (expense), net	607	(294)	(879)	(527)	(368)
Income (loss) from continuing operations before income taxes	(1,530)	3,501	2,455	946	318
Provision (benefit) for income taxes	(468)	(379)	(2,328)	9	16
Net income (loss) from continuing operations before extraordinary item	(1,062)	3,880	4,783	937	302
Loss from operations of discontinued division, net of tax	(226)	—	(876)	(562)	(1,746)
Loss from disposal of discontinued division, net of tax	—	—	(2,032)	—	—
Net income (loss) before extraordinary item	(1,288)	3,880	1,875	375	(1,444)
Loss from early extinguishment of debt, net of tax	—	(909)	—	—	—
<b>Net income (loss)</b>	<b>\$ (1,288)</b>	<b>\$ 2,971</b>	<b>\$ 1,875</b>	<b>\$ 375</b>	<b>\$ (1,444)</b>
 Net income (loss) from continuing operations before extraordinary item per share:					
<b>Basic</b>	<b>\$ (0.10)</b>	<b>\$ 0.53</b>	<b>\$ 2.17</b>	<b>\$ 0.15</b>	<b>\$ (0.02)</b>
<b>Diluted</b>	<b>\$ (0.10)</b>	<b>\$ 0.38</b>	<b>\$ 0.54</b>	<b>\$ 0.11</b>	<b>\$ (0.02)</b>
 Net income (loss) per share:					
<b>Basic</b>	<b>\$ (0.12)</b>	<b>\$ 0.39</b>	<b>\$ 0.61</b>	<b>\$ (0.17)</b>	<b>\$ (1.07)</b>
<b>Diluted</b>	<b>\$ (0.12)</b>	<b>\$ 0.29</b>	<b>\$ 0.21</b>	<b>\$ 0.05</b>	<b>\$ (1.07)</b>
 Cash and cash equivalents	\$ 8,354	\$ 10,266	\$ 2,503	\$ 32	\$ 1,004
Short and long-term investments in marketable securities	13,158	9,815	—	—	—
Working capital (deficit)	18,014	17,678	(2,670)	(7,345)	(8,135)
Total assets	41,780	45,095	21,106	18,482	11,755
Long-term debt	2,038	2,791	6,891	3,318	1,934
Total stockholders' equity (deficit)	32,935	33,591	(11,867)	(13,068)	(4,614)

See Note 2 of Notes to Financial Statements for an explanation of the determination of the shares used in computing net income (loss) per share.

## Management's Discussion and Analysis of Financial Condition and Results of Operations

This Annual Report contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, (1) lengthy sales cycles associated with our services and products, (2) our reliance on large contracts from a limited number of significant customers, (3) rate of adoption of 9-1-1 technology by wireless carriers, (4) continuing rapid change in the telecommunications industry that may affect us and our customers, (5) continuing demand for our services and products, and (6) additional factors described in our Annual Report on Form 10-K for the year ended December 31, 1999.

### Overview

Prior to 1995, substantially all of our revenue was derived from the sale of software licenses and related implementation services to ILECs and public safety agencies. During 1994, we began investing in infrastructure to provide our 9-1-1 OSS<sup>SM</sup> solution to telephone operating companies seeking to outsource such operations. We signed our first 9-1-1 data management services contract in August 1994 and continue to add to the number of records under management. We began to recognize revenue from wireless carriers in the third quarter of 1997, and continue to increase the number of live wireless subscribers managed. In addition, we signed a contract with the General Services Commission of the State of Texas in November 1998, representing the first time that a state agency has endeavored to centralize 9-1-1 OSS and data management services with a neutral third party.

Our data management services revenue is derived from contracts with ILECs, CLECs, wireless carriers and a state agency pursuant to which we provide an outsourcing solution for our customers' 9-1-1 data management. Revenue included in data management services generally includes a non-recurring fee for the design and implementation of the 9-1-1 OSS, conversion of the customer's data to our systems, hiring and training of personnel, and other costs required to prepare for the processing of customer data. Non-recurring fees are recognized on the percentage-of-completion method over the period required to perform the tasks necessary to prepare for the processing of customer data. Our contracts also separately allow for a monthly service fee based on the number of subscriber records under management, which is recognized in the period in which the services are rendered. Data management services revenue also may include revenue from enhanced products and services, which may include non-recurring and/or monthly fees which are separately stated in the contract and are recognized in the period in which the services are performed. Related costs are expensed as they are incurred. Data management services revenue comprised 99% of our total revenue in 1999 and 89% in each of the years ended December 31, 1998 and 1997.

Our licenses and implementation services revenue is derived from contracts with ILECs pursuant to which we provide a 9-1-1 software license or related products and services such as implementation, training, software enhancements and interfaces to our customers' systems. Licenses and implementation services revenue is recognized using the percentage-of-completion method. The related costs include third-party licenses, direct labor and related expenses, and are expensed as incurred. Subsequent to system installation, we provide our customers with maintenance services that are recognized ratably over the related contract period on a straight-line basis. Our licenses and implementation services revenue is derived from a limited number of customers and consequently the concentration of customers can result in quarterly fluctuations based on the

timing of the signing of new contracts and completion of existing contracts. Margins on such contracts also may fluctuate based on the elements included in the contract. We completed the licenses and implementation services contracts we had in place in 1998 and did not sign additional contracts due to our focus on our longer term services contracts. We do not expect to generate significant revenue from licenses and implementation services during 2000. Licenses and implementation services revenue comprised 1% of our total revenue in 1999 and 11% in each of the years ended December 31, 1998 and 1997.

During the year ended December 31, 1999, we recognized approximately 81% of total revenue from Ameritech, BellSouth Inc. and U S WEST, each of which accounted for greater than 10% of our total revenue. During the year ended December 31, 1998, we recognized approximately 73% of total revenue from Ameritech, BellSouth Inc. and U S WEST, each of which accounted for greater than 10% of our total revenue.

During the year ended December 31, 1997, we recognized approximately 81% of total revenue from continuing operations from Ameritech, BellSouth Inc. and U S WEST, each of which accounted for greater than 10% of our total revenue.

In the third quarter of 1998, one of our licenses and implementation services customers, Bell Atlantic, who had merged with Nynex, announced their decision to standardize their 9-1-1 hardware and software platform utilizing non-SCC systems that had been used by Nynex prior to the merger. In the fourth quarter of 1998, we entered into a Termination, Settlement and Release Agreement with Bell Atlantic, under which Bell Atlantic paid us for work that had been performed prior to cancellation of the contract. This transition occurred over the course of 1999, during which time we continued to support the systems installed in Bell Atlantic and cooperated fully to ensure a smooth transition of these systems. Bell Atlantic comprised approximately 8% of our total revenue in 1998.

As of December 31, 1999, we had net operating loss carry forwards of \$11.2 million available to offset future net income for U.S. federal income tax purposes. We reversed \$1.7 million of the valuation allowance on our deferred tax assets in the year ended December 31, 1998 and recorded an additional income tax benefit of \$468,000 from continuing operations in the year ended December 31, 1999, as we believe that it is more likely than not that such tax benefits will be realized. Of the \$912,000 tax benefit recorded in 1998, \$533,000 related to the extraordinary loss from early extinguishment of debt. We expect to incur losses in the near term related to development costs for new commercial products and future taxable income may not be sufficient to realize additional deferred tax assets that will be created by the projected net operating losses. Consequently, we presently expect our statement of operations will not reflect tax benefits for projected operating losses to be incurred during 2000.

In June 1997, we sold the net assets of our Premise Products Division. The sale of our Premise Products Division resulted in a net loss from the sale of \$2.0 million. Net losses from operations of this division totaled \$876,000 and \$226,000 in 1997 and 1999, respectively, and are presented in our financial statements as loss from operations of discontinued division. The loss from discontinued operations in 1999 resulted from final closeout of unassigned contracts and the transition of customers to the company that acquired this division.

In June and July 1998, we completed an initial public offering of our common stock, which generated proceeds of \$26.0 million, net of the underwriter's discount and other offering costs and including the exercise of the underwriters' over allotment option. See Note 2 to the accompanying financial



statements and "Liquidity and Capital Resources."

Historically, substantially all of our revenue has been generated from sales to customers in the United States. However, we have generated revenue in Canada and intend to enter additional international markets, which may require significant management attention and financial resources. International sales are subject to a variety of risks.

Our quarterly and annual operating results have varied significantly in the past. The variation in operating results will likely continue and may intensify. We believe that period to period comparisons of results of operations are not necessarily meaningful and should not be relied upon as indications of future performance. Our operating results may continue to fluctuate as a result of many factors, including the length of the sales cycles for new or existing customers, the size, timing or duration of significant customer contracts, fluctuations in number of subscriber records under management, timing or duration of service offerings, rate of adoption of wireless services by Public Safety Answering Points, efforts expended to accelerate the introduction of certain new products, our ability to hire, train and retain qualified personnel, increased competition, changes in operating expenses, changes in our strategy, the financial performance of our customers, changes in telecommunications legislation and regulations that may affect the competitive environment for our services, and general economic factors. Our contracts for 9-1-1 OSS services generally include a separate non-recurring fee for the design and implementation of the 9-1-1 OSS, conversion of the customer's data to our systems, hiring and training of personnel, and other costs required to prepare for the processing of customer data, and therefore, we may recognize significantly increased revenue for a short period of time upon commencing services for a new customer.

Our expense levels are based in significant part on our expectations regarding future revenue. Our revenue is difficult to forecast because the market for our services is evolving rapidly and the length of our sales cycle, the size and timing of significant customer contracts and license fees and the timing of recognition of non-recurring initial fees vary substantially among customers. Accordingly, we may be unable to adjust spending in a timely manner to compensate for any unexpected shortfall in revenue. Any significant shortfall could therefore have a material adverse effect on our business, financial condition and results of operations. We will incur expenses of approximately \$10 million in 2000 for research, development and marketing to expand our product offerings. In addition, we hired additional employees in 1999, 1998 and 1997, and expect to continue hiring additional employees during 2000. We also began leasing office space in Texas in December 1999, from which we will perform some of our operations. We cannot assure you that we can report operating profits or that our investments in research and development will generate future revenue. Failure to do so could have a material adverse effect on our business, financial condition and results of operations.

#### Results of Operations

##### Year Ended December 31, 1999 Compared to Year Ended December 31, 1998

#### Revenue

**Total Revenue.** Total revenue decreased 5%, from \$34.4 million in 1998 to \$32.6 million in 1999.

**Data Management Services Revenue.** Revenue from data management services increased 5%, from \$30.6 million in 1998 to \$32.1 million in 1999, representing approximately 89% and 99% of total revenue, respectively. Data management services revenue increased due to an increase in the number of records under management for ILEC and CLEC customers caused by

customer growth and the signing of additional CLEC contracts. These increases were offset by monthly minimum fees from a wireless carrier in 1998 that expired at the end of 1998 and a decrease in non-recurring fees related to wireless and wireline services.

**Licenses and Implementation Services.** Revenue from licenses and implementation services decreased 87%, from \$3.8 million in 1998 to \$488,000 in 1999, as we had no licenses and implementation services contracts in process in 1999 other than warranty contracts.

#### Costs and Expenses

**Cost of Data Management Services.** Cost of data management services consists primarily of labor and costs of interconnection with customers' systems and our infrastructure. Cost of data management services increased 17%, from \$20.7 million in 1998 to \$24.3 million in 1999, representing 60% and 75% of total revenue, respectively, and 68% and 76% of data management services revenue, respectively. The dollar increase was due to the pilot phase and start of implementation of our contract with the State of Texas, increased depreciation expense and telephone lines to accommodate growth in our wireless and wireline operations, and additional headcount and related costs incurred to accommodate growth for both wireline and wireless services. The percentage increase occurred primarily because the rollout of our wireless and enhanced services has been slower than anticipated, although we have built the infrastructure to service the anticipated demand, and the infrastructure required to begin the State of Texas contract before significant revenue was generated. In addition, in 1998, we received monthly minimum fees from a wireless customer which expired at the end of 1998.

**Cost of Licenses and Implementation Services.** Cost of licenses and implementation services consists primarily of labor, license fees for third party software and related expenses. Cost of licenses and implementation services decreased 83%, from \$836,000 in 1998 to \$139,000 in 1999, representing 2% and 0.4% of total revenue, respectively, and 22% and 28% of licenses and implementation services revenue, respectively. The dollar decrease occurred because we had no licenses and implementation services contracts in process during 1999 other than warranty contracts.

**Sales and Marketing.** Sales and marketing expenses consist primarily of expenses related to salaries and commissions, travel, trade shows and sales collateral. Sales and marketing expenses increased 29%, from \$4.1 million in 1998 to \$5.3 million in 1999, representing 12% and 16% of total revenue, respectively. The dollar increase was due to the addition of marketing personnel, the creation of a government affairs department to interpret and influence legislation primarily related to our wireless operations and related legal expenses, addition of sales staff for enhanced services and an increase in tradeshow expenses.

**General and Administrative.** General and administrative expenses consist primarily of expenses related to our information systems, finance, human resources, legal, executive and financial planning departments. General and administrative expenses decreased 1%, from \$5.0 million in 1998 to \$4.9 million in 1999, representing 14% and 15% of total revenue, respectively. We experienced decreases due to a decrease in expenses related to the resignations of our chief operating officer and chief financial officer. These decreases were partially offset by:

- the addition of information technology personnel and related expenses;
- increased legal and accounting costs related to quarterly and annual reporting requirements as we became a publicly traded company in June 1998;

increased legal staffing and other fees related to regulatory and legislative issues concerning the implementation of our services in Texas; and

the creation of an investor relations department.

**Other Income (Expense), Net.** Net other income (expense) consists primarily of interest expense from our borrowings and leases for capital equipment, offset by interest income earned on our cash and investment balances. Net other expense was \$294,000 in 1998 compared to net other income of \$607,000 in 1999, representing (1)% and 2% of total revenue for such periods, respectively. The dollar increase in net other income was primarily due to a decrease in interest expense related to the repayment of certain bank debt outstanding through the second quarter of 1998 and repayment of certain capital leases and an increase in interest earned from the investment of funds received from our initial public offering in June and July of 1998.

**Benefit for Income Taxes.** Our income tax benefit from continuing operations increased from \$379,000 in 1998 to \$468,000 in 1999. In 1998, we reversed a portion of our valuation allowance and in 1999 recorded an income tax benefit related to our deferred tax assets as we believe that it is more likely than not that the tax assets will be realized.

**Loss from Operations of Discontinued Division.** We recorded a charge of \$226,000 in 1999, net of the related tax benefit, related to the final closeout of unassigned contracts and the transition of customers to the company that acquired this division.

**Loss from Early Extinguishment of Debt.** We recorded a charge of \$909,000 in 1998, net of the related tax benefit, related to the write-off of the remaining debt discount and other costs associated with the early extinguishment of our bank debt.

#### **Year Ended December 31, 1998 Compared to Year Ended December 31, 1997**

#### **Revenue**

**Total Revenue.** Total revenue increased 27%, from \$27.1 million in 1997 to \$34.4 million in 1998.

**Data Management Services Revenue.** Revenue from data management services increased 28%, from \$24.0 million in 1997 to \$30.6 million in 1998, representing approximately 89% of total revenue in both periods. The increase resulted primarily from increases in:

- monthly fees from wireline customers due to an increase in the number of subscribers under management;
- non-recurring and monthly fees from wireless customers, as we did not begin to earn revenue from wireless customers until the third quarter of 1997 and signed several new contracts in 1998;
- non-recurring fees from enhanced services; and
- non-recurring fees from new wireline customers that were transitioned to our systems.

**Licenses and Implementation Services.** Revenue from licenses and implementation services increased 25%, from \$3.1 million in 1997 to \$3.8 million in 1998, due to increased work performed on contracts that began in 1997 and were completed or terminated during 1998.

#### **Costs and Expenses**

**Cost of Data Management Services.** Cost of data management services increased 35%, from \$15.4 million in 1997 to \$20.7 million in 1998, representing 57% and 60% of total revenue, respectively, and 64% and 68% of

data management services revenue, respectively. The dollar increase was due to the addition of personnel and equipment and expansion of facilities to accommodate growth in our wireless and wireline operations.

**Cost of Licenses and Implementation Services.** Cost of licenses and implementation services decreased 35%, from \$1.3 million in 1997 to \$836,000 in 1998, representing 5% and 2% of total revenue, respectively, and 42% and 22% of licenses and implementation services revenue, respectively. The decrease in dollars and as a percent of licenses and implementation services revenue was primarily due to the reversal of accrued third party software fees that will not be required and an increase in warranty revenue, both of which resulted from the cancellation of our contract with Bell Atlantic.

**Sales and Marketing.** Sales and marketing expenses increased 7%, from \$3.9 million in 1997 to \$4.1 million in 1998, representing 14% and 12% of total revenue, respectively. The increase was primarily due to salaries and related costs of hiring additional sales and marketing personnel during 1998 and public relations costs incurred in 1998. These increases were partially offset by decreases in sales commissions, as well as the transfer of a vice president to a general and administrative position.

**General and Administrative.** General and administrative expenses increased 54%, from \$3.2 million in 1997 to \$5.0 million in 1998, representing 12% and 14% of total revenue, respectively. The dollar increase was due to:

- the reassignment of certain continuing resources, infrastructure and related general and administrative expenses applicable to continuing operations;
- addition of personnel and computer equipment in the accounting, information systems, legal and human resources departments to support our growth;
- the transfer of a marketing vice president to a general and administrative position; and
- strategic consulting costs incurred in 1998.

The increases were partially offset by a decrease in executive bonuses.

**Other Expenses, Net.** Other expenses decreased 67%, from \$879,000 in 1997 to \$294,000 in 1998, representing 3% and 1% of total revenue, respectively. The dollar decrease was primarily due to the repayment of certain bank debt and capital leases during 1998 and interest earned from the investment of funds from our initial public offering in June and July of 1998.

**Income Tax Benefit.** The income tax benefit of \$379,000 in 1998 consists of the reversal of a portion of our valuation allowance on our deferred tax assets, compared to a reversal of valuation allowance of \$2.4 million in 1997. We did not record a state income tax provision in 1998 primarily due to the utilization of state net operating loss carry forwards. In 1997, we recorded a state provision of \$172,000 as more business was conducted in states where net operating loss carryforwards were not available.

**Loss from Sale and Operations of Discontinued Division.** In 1997, we recorded a charge of \$2.9 million, net of the related tax effect, related to the sale of the net assets of our Premise Products Division.

**Loss from Early Extinguishment of Debt.** We recorded a charge of \$909,000 in 1998, net of the related tax benefit, related to the write-off of the remaining debt discount and other costs associated with the early extinguishment of our bank debt.



*Liquidity and Capital Resources*

Since our inception we have funded our operations with cash provided by operations, supplemented by equity and debt financing and leases on capital equipment. As of December 31, 1999, we had \$21.5 million in cash and cash equivalents and investments in marketable securities.

In June 1998, we completed an initial public offering of 2,100,000 shares of our common stock, which generated proceeds of \$22.5 million to us, net of the underwriter's discount and other offering costs. We used approximately \$4.4 million of the proceeds to repay our bank loans and \$160,000 for the related prepayment penalty. In July 1998, the underwriters of our initial public offering exercised their over-allotment option. Under the over-allotment option, we sold an additional 315,000 shares of our common stock, generating net proceeds of \$3.5 million.

In addition to the \$4.4 million of debt repaid with the proceeds of the initial public offering, we repaid \$5.6 million and \$1.9 million of other bank debt and capital lease obligations during 1998 and 1999, respectively. Additionally, we used \$3.4 million and \$2.5 million during 1998 and 1999, respectively, for the purchase of capital assets and software development. We anticipate that our level of spending for capital expenditures in 1999 will continue during 2000, although we currently have no material commitments for capital expenditures.

We have a line of credit with a bank equal to \$2.0 million, which is available to meet operating needs. The interest rate on amounts borrowed under the line of credit is equal to the bank's prime rate or the one, two or three month Libor rate plus 2.25% per annum. The line of credit matures April 15, 2000 and is collateralized by certain of our assets. As of December 31, 1999, no borrowings were outstanding on the line of credit.

We also have a \$2.0 million capital lease line with a bank which is available to meet capital acquisition needs that arise from normal business operations. The interest rate on capital leased under the lease line is equal to the bank's cost of funds at the time of each lease. Separate lease schedules are signed from time to time. Each lease schedule is collateralized by the assets that are being leased. Each lease has its own termination date, typically 36 months. As of December 31, 1999, \$582,000 was outstanding on the capital lease line.

We have announced plans to incur research, development and marketing expenses of approximately \$10 million to expand our product offerings. This will require approximately \$13 million in cash due to the capital expenditure requirements. We may also increase our capital lease line to finance this initiative. We believe that our remaining net proceeds from our initial public offering, cash generated from operations and lease financing will be sufficient to fund our anticipated working capital needs, research and development initiative, capital expenditures and any potential future acquisitions through at least the next twelve months. In the event our plans or assumptions change or prove to be inaccurate, or if we consummate any unplanned acquisitions of businesses or assets, we may be required to seek additional sources of capital. Sources of additional capital may include public and private equity and debt financings, sales of nonstrategic assets and other financing arrangements.

*Year 2000 Capability*

Many currently installed computer and software products were coded to accept only two digit entries in the date code field. These date code fields need to accept four digit entries to distinguish twenty-first century dates from twentieth century dates. We use off-the-shelf and custom software

developed internally and by third parties for our production, information technology (IT) and non-IT systems.

We programmed and tested our systems and installed all upgrades necessary to make them Year 2000 compliant. We spent about \$400,000 to make our systems Year 2000 compliant. As a result of our Year 2000 readiness efforts, our production systems, IT systems and non-IT systems successfully distinguished twenty-first century dates from twentieth century dates on January 1, 2000 without any system failures. However, we are continuing to monitor our systems throughout the year 2000 to ensure that any latent Year 2000 matters that may arise are addressed promptly. Despite the fact that many companies' software and computer systems are currently processing twenty-first century dates correctly, these companies, including us, could experience latent Year 2000 problems.

*Recently Issued Accounting Pronouncements***Statement of Financial Accounting Standards No. 133 and No. 137**

In June 1998, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS 133 establishes accounting and reporting standards for derivative financial instruments and hedging activities related to those instruments as well as other hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities in the statement of financial position and measures those instruments at fair value. In June 1999, the FASB issued Statement of Financial Accounting Standards No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133 - An amendment of FASB Statement No. 133." SFAS No. 137 delays the effective date of SFAS No. 133 to financial quarters and financial years beginning after June 15, 2000. We do not typically enter into arrangements that would fall under the scope of Statement No. 133 and thus, management believes that Statement No. 133 will not significantly affect our financial condition and results of operations.

**Statement of Position 98-9**

In December 1998, the American Institute of Certified Public Accountants issued Statement of Position 98-9, "Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions." SOP 98-9 amends certain paragraphs of Statement of Position 97-2, "Software Revenue Recognition," to require the application of a residual method of accounting for software revenue when certain conditions exist. SOP 98-9 also amends Statement of Position 98-4, "Deferral of the Effective Date of a Provision of SOP 97-2" to extend the deferral of the application of certain passages of SOP 97-2 provided by SOP 98-4 through fiscal years beginning on or before March 15, 1999. All other provisions of SOP 98-9 are effective for transactions entered into in fiscal years beginning after March 15, 1999. Earlier adoption is permitted; however, retroactive application is prohibited. We believe SOP 98-9 will not materially impact our financial statements.

**Staff Accounting Bulletin No. 101**

In December 1999, the Securities and Exchange Commission staff released Staff Accounting Bulletin No. 101, "Revenue Recognition." SAB 101 provides interpretive guidance on the recognition, presentation and disclosure of revenue in financial statements. SAB 101 must be applied to financial statements no later than the second fiscal quarter of 2000. We are currently reviewing SAB 101 to determine what impact, if any, the adoption of SAB 101 will have on our financial position and results of operations.

Balance Sheets <i>(dollars in thousands)</i>	December 31,	
	1999	1998
Current assets:		
Cash and cash equivalents	\$ 8,354	\$ 10,266
Short-term investments in marketable securities	12,165	7,761
Accounts receivable, net of allowance of approximately \$58 and \$50 in 1999 and 1998, respectively, for doubtful accounts	2,255	4,820
Unbilled revenue	846	1,035
Prepays and other	548	484
Deferred income taxes — current portion	653	2,025
Total current assets	24,821	26,391
Property and equipment, at cost:		
Computer hardware and equipment	25,411	23,687
Furniture and fixtures	933	800
Leasehold improvements	915	920
	27,259	25,407
Less — Accumulated depreciation	(15,753)	(11,056)
Total property and equipment	11,506	14,351
Other assets	86	112
Long-term investments in marketable securities	993	2,054
Deferred income taxes — noncurrent	3,423	1,504
Software development costs, net of accumulated amortization of \$575 and \$346 in 1999 and 1998, respectively	951	683
	<b>\$ 41,780</b>	<b>\$ 45,095</b>
Current liabilities:		
Accounts payable	\$ 752	\$ 1,211
Payroll-related accruals	786	734
Other accrued liabilities	1,641	2,546
Property and other taxes	792	696
Current portion of capital lease obligations (Note 5)	1,971	1,618
Deferred contract revenue	865	1,908
Total current liabilities	6,807	8,713
Long-term debt:		
Capital lease obligations, net of current portion (Note 5)	2,038	2,791
Total liabilities	8,845	11,504
Commitments and contingencies (Notes 7 and 11)		
Stockholders' Equity (Note 4):		
Preferred stock, \$.001 par value; 15,000,000 shares authorized; none issued or outstanding	—	—
Common stock, \$.001 par value; 30,000,000 shares authorized; 11,104,111 and 10,886,353 shares issued at December 31, 1999 and 1998, respectively	11	10
Additional paid-in capital	43,925	43,320
Stock subscriptions receivable	(33)	(59)
Accumulated deficit	(10,968)	(9,680)
Total stockholders' equity	32,935	33,591
	<b>\$ 41,780</b>	<b>\$ 45,095</b>

The accompanying Notes to Financial Statements are an integral part of these balance sheets.

# Statements of Operations

	Year Ended December 31,		
	1999	1998	1997
Statements of Operations (dollars in thousands, except per share data)			
Revenue:			
Data management services	\$ 32,096	\$ 30,610	\$ 24,005
Licenses and implementation services	488	3,839	3,067
Total revenue	32,584	34,449	27,072
Cost and expenses:			
Cost of data management services	24,338	20,740	15,378
Cost of licenses and implementation services	138	836	1,283
Sales and marketing	5,314	4,119	3,850
General and administrative	4,931	4,959	3,227
Total costs and expenses	34,721	30,654	23,738
Income (loss) from operations	(2,137)	3,795	3,334
Other income (expense):			
Interest and other income	1,095	654	88
Interest and other expense	(488)	(948)	(967)
Income (loss) from continuing operations before income taxes and extraordinary item	(1,530)	3,501	2,455
Benefit for income taxes (Note 6)	(468)	(379)	(2,328)
Net income (loss) from continuing operations before extraordinary item	(1,062)	3,880	4,783
Discontinued operations (Note 3):			
Loss from operations of discontinued division, net of tax	(226)	—	(876)
Loss from disposal of discontinued division, net of tax	—	—	(2,032)
Net income (loss) before extraordinary item	(1,288)	3,880	1,875
Extraordinary loss from early extinguishment of debt, net of tax	—	(909)	—
<b>Net income (loss)</b>	<b>\$ (1,288)</b>	<b>\$ 2,971</b>	<b>\$ 1,875</b>
Dividends accrued on Series D, E and F mandatorily redeemable convertible preferred stock	—	(355)	(740)
Common stock warrant put price adjustment	—	(77)	(8)
<b>Net income (loss) applicable to common stock</b>	<b>\$ (1,288)</b>	<b>\$ 2,539</b>	<b>\$ 1,127</b>
Net income (loss) per share from continuing operations before extraordinary item (Note 2):			
Basic	\$ (0.10)	\$ 0.53	\$ 2.17
Diluted	\$ (0.10)	\$ 0.38	\$ 0.54
Net income (loss) per share before extraordinary item (Note 2):			
Basic	\$ (0.12)	\$ 0.53	\$ 0.61
Diluted	\$ (0.12)	\$ 0.38	\$ 0.21
Net income (loss) per share (Note 2):			
Basic	\$ (0.12)	\$ 0.39	\$ 0.61
Diluted	\$ (0.12)	\$ 0.29	\$ 0.21
Shares used in computing net income (loss) per share (Note 2):			
Basic	10,989,091	6,433,564	1,857,413
Diluted	10,989,091	10,334,556	8,788,816

The accompanying Notes to Financial Statements are an integral part of these statements.

# Statements of Stockholders' Equity (Deficit)

## Statements of Stockholders' Equity (Deficit)

(dollars in thousands, except per share data)

Statements of Stockholders' Equity (Deficit)	Common Stock		Additional Paid-in Capital	Stock Subscriptions Receivable		Treasury Stock	Accumulated Deficit	Total Stockholders' Equity (deficit)
(dollars in thousands, except per share data)								
BALANCES, at December 31, 1996	1,840,899	\$ 2	\$ 298	\$ (19)	(36,250)	\$ (3)	\$ (13,346)	\$ (13,068)
Dividends accrued on Series D, E and F Convertible Preferred Stock	—	—	—	—	—	—	(740)	(740)
Exercise of stock options, including options exercised in exchange for notes receivable	153,382	—	154	(80)	—	—	—	74
Common stock warrant put price adjustment (Note 4)	—	—	—	—	—	—	(8)	(8)
Net income	—	—	—	—	—	—	1,875	1,875
BALANCES, at December 31, 1997	1,994,281	2	452	(99)	(36,250)	(3)	(12,219)	(11,867)
Dividends accrued on Series D, E and F Convertible Preferred Stock	—	—	—	—	—	—	(355)	(355)
Issuance of common stock through Initial Public Offering, net of issuance costs of \$964	2,415,000	2	25,985	—	—	—	—	25,987
Conversion of preferred stock into common stock	6,188,575	6	14,938	—	—	—	—	14,944
Conversion of common stock warrants	195,148	—	1,549	—	—	—	—	1,549
Issuance of common stock under Employee Stock Purchase Plan	61,105	—	243	—	—	—	—	243
Exercise of stock options	68,494	—	39	—	—	—	—	39
Common stock warrant put price adjustment	—	—	—	—	—	—	(77)	(77)
Stock subscription payments received	—	—	—	40	—	—	—	40
Tax benefit related to disqualifying dispositions of common stock	—	—	117	—	—	—	—	117
Retirement of treasury stock	(36,250)	—	(3)	—	36,250	3	—	—
Net income	—	—	—	—	—	—	2,971	2,971
BALANCES, at December 31, 1998	10,886,353	10	43,320	(59)	—	—	(9,680)	33,591
Issuance of common stock under Employee Stock Purchase Plan	38,679	—	145	—	—	—	—	145
Exercise of stock options	179,079	1	460	—	—	—	—	461
Stock subscription payments received	—	—	—	26	—	—	—	26
Net loss	—	—	—	—	—	—	(1,288)	(1,288)
BALANCES, at December 31, 1999	11,104,111	\$11	\$43,925	\$ (33)	—	\$—	\$ (10,968)	\$ 32,935

The accompanying Notes to Financial Statements are an integral part of these statements.

	Year Ended December 31,		
Statements of Cash Flows (dollars in thousands)	1999	1998	1997
Cash flows from operating activities:			
Net income (loss)	\$ (1,288)	\$ 2,971	\$ 1,875
Adjustments to reconcile net income to net cash provided by operating activities —			
Amortization and depreciation	5,117	4,315	3,534
Amortization and write-off of note payable discount	—	1,430	33
Accretion of investments in marketable securities	(284)	(316)	—
(Gain) loss on disposal of assets	53	—	(40)
Loss on disposal of discontinued division	—	—	2,032
Provision for estimated losses on contracts	—	7	(196)
Provision for doubtful accounts	8	—	25
Deferred income tax benefit	(547)	(912)	(2,500)
Change in —			
Accounts receivable	2,557	(2,492)	(977)
Unbilled revenue	189	(39)	(190)
Prepays and other	(38)	(286)	(202)
Accounts payable	(29)	246	236
Accrued liabilities	(433)	150	1,337
Deferred contract revenue	(1,043)	(705)	303
Decrease in current assets and liabilities from discontinued operations	—	—	110
Net cash provided by operating activities	4,262	4,369	5,380
Cash flows from investing activities:			
Acquisition of property and equipment	(1,961)	(2,995)	(2,646)
Proceeds from sale of net assets	—	—	603
Purchase of investments in marketable securities	(14,559)	(14,446)	—
Sale of investments in marketable securities	11,500	4,947	—
Software development costs	(497)	(397)	(142)
Net cash used in investing activities	(5,517)	(12,891)	(2,185)
Cash flows from financing activities:			
Proceeds from issuance of notes payable	—	—	4,275
Principal payments on notes payable	—	(4,986)	(1,439)
Principal payments on capital lease obligations	(1,870)	(5,038)	(3,634)
Proceeds from equipment financing	581	—	—
Exercise of stock options	461	39	74
Stock subscription payments received	26	40	—
Purchases through employee stock purchase plan	145	243	—
Proceeds from initial public offering and overallotment, net of underwriters' discount	—	26,951	—
Costs related to initial public offering	—	(964)	—
Net cash provided by (used in) financing activities	(657)	16,285	(724)
Net increase (decrease) in cash and cash equivalents	(1,912)	7,763	2,471
Cash and cash equivalents, beginning of period	10,266	2,503	32
Cash and cash equivalents, end of period	\$ 8,354	\$10,266	\$ 2,503
Supplemental disclosure of cash flow information:			
Cash paid during the period for interest	\$ 439	\$ 801	\$ 942
Cash paid during the period for taxes	\$ 459	\$ 95	\$ 18
Supplemental schedule of noncash financing and investing activities:			
Dividends accrued on Series D, E and F Convertible Preferred Stock	\$ —	\$ 355	\$ 740
Common stock issued to employees in exchange for employee notes receivable	\$ —	\$ —	\$ 80
Property acquired with capital leases	\$ 889	\$ 3,488	\$ 3,074
Conversion of preferred stock	\$ —	\$14,943	\$ —
Conversion of warrants	\$ —	\$ 1,549	\$ —
Retirement of treasury stock	\$ —	\$ 3	\$ —

The accompanying Notes to Financial Statements are an integral part of these statements.

## Notes to Financial Statements

### (1) Organization, Business and Liquidity

SCC Communications Corp. (the "Company") is a Delaware corporation. The Company is the leading provider of 9-1-1 operations support systems services to incumbent local exchange carriers ("ILECs"), competitive local exchange carriers ("CLECs"), wireless carriers and state and local governments in the United States. The Company manages the data which enables 9-1-1 calls to be routed to the appropriate public safety agency with accurate and timely information about the caller's identification and location. In addition, the Company licenses its 9-1-1 software to carriers that wish to manage the delivery of 9-1-1 data management services in-house.

### (2) Summary of Significant Accounting Policies Operating Cycle

Assets and liabilities related to contracts are included in current assets and liabilities in the accompanying balance sheets since they will be liquidated in the normal course of contract completion, although this may require more than one year.

### Property and Equipment

Depreciation of property and equipment is computed using the straight-line method over estimated useful lives of three to five years for computer hardware and equipment, seven years for furniture and fixtures and the life of the lease for leasehold improvements. The costs of repairs and maintenance are expensed while enhancements to existing assets are capitalized. Depreciation expense totaled approximately \$4,888,000, \$4,174,000 and \$3,399,000 for the years ended December 31, 1999, 1998 and 1997, respectively.

### Software Development Costs

The Company expenses the costs of developing computer software until technological feasibility is established and capitalizes all costs incurred from that time until the software is available for general customer release. Technological feasibility for the Company's computer software products is based upon the earlier of the achievement of (a) a detailed program design free of high-risk development issues or (b) completion of a working model. Costs of major enhancements to existing products with a wide market are capitalized while routine maintenance of existing products is charged to expense as incurred. The establishment of technological feasibility and the ongoing assessment of the recoverability of capitalized computer software development costs requires considerable judgment by management with respect to certain external factors, including, but not limited to, technological feasibility, anticipated future gross revenue, estimated economic life and changes in software and hardware technology.

Capitalized software costs are amortized on a product-by-product basis. The annual amortization is the greater of the amount computed using (a) the ratio that current gross revenue for a product compares to the total of current and anticipated future gross revenue for that product, or (b) the straight-line method over the remaining estimated economic life of the product which is typically five years. Amortization expense related to capitalized software costs totaled approximately \$229,000, \$145,000 and \$107,000 for the years ended December 31, 1999, 1998 and 1997, respectively, and is included in cost of data management services and licenses and implementation services in the statements of operations.

### Revenue Recognition

The Company reports revenue based on its two segments, data management services and licenses and implementation services.

Revenue from data management services generally consists of a non-recurring fee and monthly recurring revenue. Revenue included in data management services generally includes a non-recurring fee for the design and implementation of the 9-1-1 OSS, conversion of the customer's data to the Company's systems, hiring and training of personnel, and other costs required to prepare for the processing of customer data. Non-recurring fees are recognized on the percentage-of-completion method over the period required to perform the tasks necessary to prepare for the processing of customer data. The Company's contracts also separately allow for a monthly service fee based on the number of subscriber records under management, which is recognized in the period in which the services are rendered. Data management services revenue also may include revenue from enhanced products and services, which may include non-recurring and/or monthly fees which are separately stated in the contract and are recognized in the period in which the services are performed.

Revenue related to software license fees and implementation of the Company's 9-1-1 systems at customer sites is recognized using the percentage-of-completion method because the Company's software requires significant modification for each customer. Such contracts include a license fee for the use of the Company's software and service fees for the installation and customization of the system. The Company's costs to install its systems include direct labor, third-party license fees and miscellaneous expenses. Such costs are included in cost of licenses and implementation services.

In applying the percentage-of-completion method, revenue and related costs are recognized based on the percentage that labor hours incurred to date compared to total estimated labor hours. Revenue recognized in excess of amounts billed is reflected as unbilled revenue and amounts billed in excess of revenue recognized are reflected as deferred contract revenue in the accompanying balance sheets. The Company recognizes any known or anticipated loss on contracts in process when such losses are determined to exist.

Revenue from licenses and implementation services includes customer support revenue which is recognized ratably over the related contract period on a straight-line basis. Costs related to customer support revenue are included in cost of licenses and implementation services in the accompanying statements of operations.

### Concentration of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk are primarily cash and cash equivalents, accounts receivable and investments in high-grade treasury bonds and commercial paper. The Company maintains its cash balances in the form of bank demand deposits, money market accounts, treasury bonds and commercial paper with original maturities less than ninety days. The Company's deposits and investments are with financial institutions that management believes are creditworthy and investments are high-grade. The Company's accounts receivable are from customers that are generally telecommunications service providers; accordingly, the Company's accounts



receivable are concentrated in the telecommunications industry. The Company's principal customers (Note 10) accounted for 71% and 30% of the Company's accounts receivable as of December 31, 1999 and 1998, respectively. The Company has no significant financial instruments with off-balance sheet risk of accounting loss, such as foreign exchange contracts, option contracts or other foreign currency hedging arrangements.

#### Research and Development

Research and development efforts consist of salaries, supplies and other related costs. These costs are expensed as incurred and totaled approximately \$1,740,000, \$1,376,000 and \$738,000 for the years ended December 31, 1999, 1998 and 1997, respectively. These costs are included in cost of data management services and licenses and implementation services in the accompanying statements of operations and do not include development costs incurred as part of the efforts performed under licenses and implementation services contracts with the Company's customers.

#### Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include highly liquid investments with original maturities of 90 days or less.

#### Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. These estimates affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

#### Fair Market Value of Financial Instruments

Financial instruments include cash and cash equivalents, corporate debt securities, accounts receivable and debt obligations. The carrying amounts for cash and cash equivalents and accounts receivable approximate fair market value because of the short maturity of these instruments. The fair value of notes are estimated based on current rates available for debt with similar maturities and securities, and at December 31, 1999 and 1998, approximates the carrying value.

#### Investments in Marketable Securities

The Company's investments in corporate debt securities are classified as held-to-maturity and are carried at the amortized cost basis. The investments had the following values at December 31, 1999 and 1998, respectively:

	Amortized/ Accreted Cost	Accrued Interest	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
Corporate Debt Securities, maturing within one year	\$ 7,761,000	\$(237,000)	\$13,000	\$(2,000)	\$7,535,000
Corporate Debt Securities, maturing after one year through five years	2,054,000	(33,000)	3,000	—	2,024,000
<b>Balances at December 31, 1998</b>	<b>\$ 9,815,000</b>	<b>\$(270,000)</b>	<b>\$16,000</b>	<b>\$ (2,000)</b>	<b>\$ 9,559,000</b>
Corporate Debt Securities, maturing within one year	\$ 12,165,000	\$ —	\$ —	\$(10,000)	\$12,155,000
Corporate Debt Securities, maturing after one year through five years	993,000	—	—	(2,000)	991,000
<b>Balances at December 31, 1999</b>	<b>\$ 13,158,000</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$(12,000)</b>	<b>\$13,146,000</b>

#### Income Taxes

The Company follows Statement of Financial Accounting Standards No. 109 ("SFAS 109"), which requires recognition of deferred income tax assets and liabilities for the expected future income tax consequences, based on enacted tax laws, of temporary differences between the financial reporting and tax basis of assets and liabilities. SFAS 109 also requires recognition of deferred tax assets for the expected future tax effects of loss carryforwards and tax credit carryforwards. Deferred tax assets are then reduced, if deemed necessary, by a valuation allowance for the amount of any tax benefits which, on a more likely than not basis, are not expected to be realized (Note 6).

#### Stock Based Compensation Plans

The Company applies APB Opinion No. 25, "Accounting for Stock Issued to Employees," ("APB Opinion No. 25") in accounting for its stock option and other stock-based compensation plans for employees and directors. The Company has adopted the disclosure provisions of Statement of Financial Accounting Standards No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation," for such options and stock-based plans for employees and directors (Note 4).